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Russian Federation

Solid Wood Products

Annual Report

2004

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Report Highlights:
Russia's production of total solid wood products is forecast to increase by 4.5 percent in 2004 and 2005, mostly in the areas of softwood lumber and hardwood plywood. Though expansion of the Russian forestry sector is still progressing slowly, the fifth consecutive year of strong overall economic growth is boosting demand from many other industries, especially the furniture and construction sectors. Russia's exports are forecast to increase for all products in 2004, though exports of low value products will still dominate.

Includes PSD Changes: Yes
Includes Trade Matrix: No
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[RS]

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Executive Summary

Production of solid wood products in Russia is forecast to increase by about 4.5 percent in 2004, boosted mostly by increased production of softwood lumber and hardwood plywood. The driving forces behind higher production are new investments in the sector aimed at increasing the competitive position of Russian products on world markets and government policies to reduce exports of unprocessed products. Additionally, the fifth consecutive year of economic growth in Russia has boosted domestic demand for most solid wood products from the construction (residential, commercial, and infrastructure starts) and from the furniture and interiors sectors. Other sectors of the economy, such as the material handling and paper and pulp industries, are also demanding more wood products. Russia's exports of forest products are also forecast to increase in most areas in 2004 and exports of low value products will still dominate Russia trade. In 2004, important changes in forest policy are expected from the State Duma regarding investments, forest certification, illegal logging, and sustainable forest and environmental management.

Production

Forest Situation/Outlook

Russia is endowed with abundant forest resources. With a total forested area estimated at 765 to 850 million hectares, Russia accounts for about one-fifth of the world's forested area and one quarter of the world's timber stock, totaling nearly 82 billion cubic meters of standing timber. Boreal forests are predominant in Russia and most forest resources are located in remote areas. It is conventional wisdom that nearly 80 percent of Russia's total forested area is in Siberia and the Far East, whereas 70 percent of the population and more than half of wood demand are in western regions of the country. Russian forests also provide the largest land-based carbon sink in the world, one of the most biodiverse ecosystems on earth, and possess strong potential to influence international trade in forest products.

However, Russia's role in world trade of forest products does not correspond to the potential of its forest resource base. Currently, Russia's share of the world market for all wood products is estimated at two to four percent and its market share of minimally processed forest products is around 22 percent. According to the Russian Union of the Forest Industry and Timber Exporters, the poor performance of the industry in Russia can be attributed to the following factors: a) lack of appropriate value-added processing capacity (most equipment is outdated); b) lack of financial support from the government; c) inefficient location of many industrial plants away from major wood supply areas; d) shortage of new investments in the forest sector due to the lack of transparent rules for potential investors; e) high export tariffs for high value forest products and high import tariffs for modern forest processing equipment; f) growing illegal turnover of forestry products, which represents a market constraint for legal exports; g) lack of enforcement of federal regulations; and h) current government policies do not support local producers of forest products. As an illustration of these problems, data for 2002 shows a decline in investment in the forest sector of $560 million versus 2001.

Solid Wood Products Situation/Outlook

Overview

Russia's economic performance once again exceeded expectations as GDP grew by 7.3 percent in 2003, compared to 4.3 percent in 2002. This is the fifth consecutive year of economic growth in Russia, though the economy continues to be heavily dependent on oil exports and neither domestic consumption nor domestic investments are strong enough to guarantee self-sustained growth.

According to the State Statistics Committee, total industrial production in Russia increased by seven percent in 2003 versus 3.7 percent the previous year. However, the forestry sector increased by only 1.5 percent. The growth of the forest industry was mostly due to the dynamic development of pulp and paper companies, while the logging sector still remains the weakest component of Russia's forest industry. Profit margins are estimated to have declined by four percent in 2003 because road and electricity fees increased, while forest products prices remained stable.

Table 1. Russian Production of Wood Products, 2001-2003

Commodity	2001	2002	2003
Cut round wood, 1,000 m3	97,000	90,200	91,800
Workable round wood, 1,000 m3	77,700	79,500	81,400
Sawn timber, 1000 m3	19,000	17,600	17,900
Window blocks, 1,000 m2	3,254	3,156	2,817
Door blocks, 1,000 m2	3,994	4,080	3,935
Ore bars, 1,000 m3	18,600	8,400	22,100
Mine boards, 1,000 m3	12,000	7,000	5,300
Plywood, 1,000 m3	1,590	1,808	1,960
Parquet, 1,000 m2	1,705	1,666	1,617
Box sets, 1,000 m3	184,000	193,200	216,000
Fiberboard, 1,000 m2	27,000	300,000	315,000
Particle board, 1,000 m3	2,482	2,732	3,181
Railway ties, 1,000 m3	4,801	4,070	3,591
Industrial Houses, 1,000 m2	90,500	135,000	65,800
Containers, pieces	12,500	8,734	9,079
Matches, 1,000 boxes	7,716	6,728	7,119
Tables, 1,000 pieces	3,665	3,751	3,574
Chairs, 1,000 pieces	3,108	3,124	2,888
Wardrobes, 1,000 pieces	2,597	2,630	2,803
Wooden beds, 1,000 pieces	630,000	627,000	662,000

Source: Russian State Statistics Committee

Temperate Hardwood and Softwood Logs

Softwood logs are the largest category of forest products production and trade in Russia. Production is forecast to increase by two percent in 2004-05 in response to higher local demand from the furniture and civil construction sectors and a slower but continued increase in exports.

Exports of softwood logs are forecast to rebound in 2004 due to growing (legal) trade with China. This followed an estimated decline of three percent in softwood log exports in 2003 because of stricter control over illegal trade with China. Major export destinations for

Russian softwood logs are China (44 percent share of total exports in 2003), Finland (19 percent), and Japan (17).

Production of temperate hardwood logs is projected to increase by seven percent in 2004 boosted by higher domestic demand from the plywood and civil construction sectors and increased exports.

Exports of hardwood logs are forecast to increase at higher rates in 2004 and 2005 because of the competitive advantage of the Russian product in major markets such as Finland (68 percent of Russia's exports of hardwood logs), China (17 percent), and Sweden (nine percent).

Hardwood and Softwood Plywood

Production of softwood plywood remains insignificant compared to hardwood plywood. An average increase of two percent in the production of softwood plywood is forecast for 2004/05 in response to small increases in the domestic furniture market. The forecast for production of hardwood plywood was revised upward in response to higher domestic and export demand. The sector lacks investment in high-tech equipment in order to produce at full capacity and with the necessary quality.

Exports of hardwood plywood are projected to increase at higher rates due to the competitiveness of the Russian product in view of the devaluation of the Russian currency in relation to the Euro. The United States and the European Union account for more than half of Russia's hardwood plywood exports.

Hardwood and Softwood Lumber

Higher production and exports of softwood lumber were increased for 2004/2005 in order to reflect higher industry expectations. Softwood lumber is projected to increase by an average rate of eight percent during 2004/05, mostly driven by booming exports and firm domestic demand.

Exports of softwood lumber are increasing at a higher rate because of the competitiveness of the Russian products and strong demand from Egypt, the European Union, and Japan. These destinations account for more than half of Russia's exports of softwood lumber.

Production of hardwood lumber is forecast to increase at a rate of two percent during 2004-05, mostly in response to increasing exports, although still at low levels in comparison with softwood lumber volumes.

Consumption

Demand for solid wood products in Russia is forecast to grow by an average of four to five percent during 2004 and 2005. This growth will be driven mostly by higher demand from the furniture, construction, housing, and infrastructure projects resulting from government incentives and programs.

According to the Ministry of Industry, Science and Technology, the Russian furniture sector has become one of the most competitive sectors of the Russian economy. In 2003, furniture production increased by 20 percent and exports increased by 12 percent in comparison with 2002. The main export markets for Russian furniture are Germany, Italy, and France. The Strategy Development Plan of the Forestry Sector of the Russian Federation for the next ten years calls for an increase of 3.5 percent per year in the furniture production capacity of the forest industry. Imports still account for a high market share in Russia (40 percent or $400 million). Although, Russian furniture can compete with foreign furniture in terms of quality and design, import tariffs have been reduced by a factor of three in 2002 for several import furniture categories, which has prompted a protectionist reaction from local industry.

Development and expansion of vertically integrated structures of large paper and pulp and wood processing enterprises will allow logging companies to decide more effectively the need for equipment renovation and price policy coordination. As a result of these changes, sawn timber output will likely increase by 11 to 14 percent in the next ten years, while particleboard and veneer will likely increase by three to four percent and six to seven percent, respectively.

Post forecasts that during 2004 and 2005, there will be an increase in demand for sawn timber, veneer, MDF and particleboard for construction, packaging materials for food, and paper bag industries.

Trade

Overview

Total exports of forest products (Chapter 44 HTS) in 2003 are forecast to reach $3.3 billion (up 15 percent from 2002), while imports of all forest products will increase by over 35 percent and reach $242 million. The increase in total value of exports of forest products can be attributed to the following factors: a) higher exports to the European Union (average increase of 26 percent in 2003 compared to 2002) because of the appreciation of the Euro; b) higher exports to Finland and Japan; and c) continued strong demand for Russia's forest products by China (although truly representative data between the two countries is difficult to obtain).

Russia remains a major exporter of logs and unprocessed forest products. In 2003, about 52 percent of all forest product exports were rough wood, which is seven percent above the previous year. Russia's exports of forest products also remain quite concentrated on China, Finland, and Japan. These countries account for over 50 percent of all Russian exports of forest products, mostly softwood logs and softwood lumber.

Exports of Russian forest products to the United States is estimated to have declined by seven percent in 2003 due to the appreciation of the ruble, affecting exports of panel products and plywood. The appreciation of the ruble increased imports of U.S. forest products by 12 percent in 2003.

Competition

Most forestry products processed in Russia cannot compete with similar foreign products. This is attributed to its poor quality product derived from the shortage of high quality processing equipment and packing. These factors decrease the value of the Russian product on the world market by 30 to 40 percent compared to the world average prices for similar forestry products. Government officials are trying to re-orient Russian producers towards exports of higher value products by attracting foreign investments to the forest sector.

Policy

Overview

One of the core issues of the “Russian Forest 2003” exhibition, that took place in Vologda in December, was “Why the forest industry generates more problems than profits in Russia?”. The answer was that the government does not have a clear and uniform policy towards the forest sector. According to the Audit Chamber of the Russian Federation, management policies for the forest sector are inconsistent at the federal level. This conclusion is the result of a recent audit for distribution of federal budget subsidies, credit, and preferences.

However, as Russia’s forests are attracting growing interest from domestic and international audiences, the forest sector has now reached center-stage of Russia’s reform agenda and the Government is remodeling the institutional and economic framework of the sector. This is envisioned by the government programs “2003-2010: Concepts for the Forest Industry” (approved in December 2002), “Forest Development” (January 2003), as well as a wave of new legal instruments currently pending approval by the State Duma.

Since September 2003, various ministries and institutions have developed more than 12 draft bills, but none of them have been approved. Several government ministries involved in forest management, such as the Ministry of Natural Resources of the Russian Federation, Ministry of Economic Development and Trade, Ministry of Industry, Science and Technology, and the Office of the President, have now joined efforts to develop a draft bill to cover issues such as rational usage, protection of forests, reforestation, and sustainable environmental resources. The draft Law on Forest Use Payments is another important document, which is to ensure effective and sustainable development of the sector. The government has included both laws in the list of priorities to be approved by the State Duma.

Recently several measures have been taken by the Government of the Russian Federation to attract foreign investment to forest sector. The most important regulations are “Investment Funds”, amendments to law on “Joint Stock Companies”, amendments to “Foreign Investments in the Russian Federation”, a law on “Leasing,” and some other legislative documents aimed at favoring foreign investments. The law on “Technical Regulation” will allow Russian industry to apply international standards, thus increasing opportunities in the export markets.

The new provisions of the Forestry Code also encourage private ownership in the industry. It is aimed at giving private investors easier access to Russia’s forests and increasing state revenue. The Code defines the type of entity that may lease timberland, which may obtain full ownership of the resource after 15 years if all lease conditions are fulfilled. The debate over implementation will be intense, as environmentalists believe that this new proposal could speed the current unsustainable exploitation of Russia’s forest.

Forest Certification

Demand for certified forestry products on European markets is estimated at 30 percent of total demand. It is expected to increase up to 50 percent in the coming years. Certification of wood products has become a market access condition for many sensitive markets in Europe, the USA, and Japan. In response, the Russian Union of Forest Industry and Timber Exporters National Council has developed a voluntary certification program for forest products. However, the implementation has been very slow. According to the Natural Resources Committee at the State Duma, it will take up to ten years to certify all forestry products in Russia. For more information on Certification please refer to GAIN Report RS3037 of 10/28/03.

Illegal Logging

According to international analysts, Russia is listed as one of several countries where illegal logging is on the rise. It is difficult to estimate the volume for unreported logging in Russia, as even the data on official logging is controversial. According to the latest official data released by the State Statistics Committee, legal logging reached 91 million cubic meters (m3) in 2002, while the Ministry of Natural Resources reported 165 million m3 for the same year. According to trade sources, 20 to 50 percent of total timber logged in Russia is unreported.

So far there is no effective legislative mechanism to curb illegal logging. Several regions of Russia developed initiatives in cooperation with local administration and institutions. Some oblasts have achieved considerable success in decreasing the volume of unreported timber logged and the other regions are building on that experience. However, it will take long time to create a system of fair reporting for the entire country. Despite intensified enforcement measures, there are not enough resources to cover all forested areas.

Forest Fires

In 2003, the most severe fires occurred in Siberia and the Far East, where 488 fires were reported. More than seven thousand fire fighters were involved in the suppression of these fires. According to the Ministry of Emergency Situations, more than two million hectares of forest were destroyed in 2003 by 547 forest fires.

Despite the fact that Russia has a great forest potential, the government is working on a reforestation program for deforested areas due to forest fires and exploitation. In 2003, the State Forest Service reported that more than 35,000 hectares of new forests were planted.

Tariffs

Since September 2003, export duties for 220 line items of high value forest products were abolished. The government is currently working on the elimination of export duties for another 180 line items of high-value products and on reducing import tariffs on equipment for logging and processing with no competitor in Russia. The decision is expected to save up to $5 billion dollars by 2015. For more information on tariffs refer to GAIN Report RS3037 of 10/28/03.

Meanwhile, the Governmental Commission on Tariff Regulation for Railroads is working on introducing a new price-list for rail shipments. The new system is expected to improve market competition for transport services, specifically by decreasing tariffs for long distance shipments and increase them for short distance. The tariffs will be unified for domestic and international routes. Currently, the railroad tariffs are growing faster than the price for the products thus decreasing profitability of most companies.

Kyoto Protocol Ratification

Russia was the center of a major controversy during the Ninth Meeting of the Parties of the United Nations Climate Change Convention conducted in Milan, Italy, in December 2003. Russia's leaders failed to reach a decision on whether to place ratification of the Kyoto Protocol before the State Duma for a vote. Since Russia accounts for 17 percent of global emissions, its support is crucial to activate the carbon gas emission control treaty. Trade sources in Russia indicated that Russia is waiting for the EU countries and Japan to show more interest in buying emission rights before ratifying the Kyoto protocol, which could then be considered after March presidential elections.

Regional Focus – Vologda

Vologda Oblast is one of the most economically developed regions of the northern part of Russia. It has well–established transportation linkages with the neighboring regions (Leningrad, Arkhangelsk, Novgorod, Yaroslavl, etc.) as well as a favorable geographical position and enormous natural resource base. The largest steel maker in Russia, Severstal, is located in Vologda Oblast and this allows more budgetary freedom in dealing with other emerging industrial sectors.

Along with highly developed steel, chemistry, and ball bearing industries, forestry is one of the leading branches of Vologda industry. Forestry products account for about seven percent of all industrial output in Vologda. Natural forests cover about 70 percent of territory of the oblast. Standing timber is calculated at 649 million m3, including 318 million m3 of coniferous species. Total annual cut is estimated at only 22 million m3. Almost 93 percent of all forestry output is produced by large and medium-sized enterprises. Forestry enterprises produce diversified products for both domestic and exports markets: softwood logs, sawn timber, plywood, veneer, doors and window, cellulose, paper, furniture, and wooden houses. Annual production in Vologda is 6,000 MT of round wood, 780 MT of sawn timber, 140 MT of veneer, 63 MT of paper, 2,653 MT of MDF and more than 150 different types of furniture. Considerable recent growth in production of sawn timber, MDF, and veneer is attributed to the booming construction and furniture industries. Competitive prices for the products from Vologda have stimulated their use by domestic industries.

The forestry sector in the region is mainly export oriented. Finland, Sweden, Norway, and the United States are the major importers of products from Vologda. Until 1996, only 38 percent of wood had been processed and more than 60 percent of all round wood was directly exported. Currently, exports of processed products have increased by 150 percent. This positive switch is attributed to efficient regional policy that provides incentive for business development. The following regional programs have been developed to help the sector: “Law on Investment Attractiveness” and “Conception of Oblast Development of 2008-2010”.

As in most forested regions of Russia, there are several crucial factors that hinder its sustainable development: low usage of resources, insufficient investment, lack of processing capacity, and depreciated equipment. However, the regional government’s strong commitment to the development of the forestry sector, abundant resources, and strategic location will continue to make Vologda a leader in Russia’s forestry sector.

Table 2. Production, Supply, and Distribution of Softwood Logs

PSD Table							
Country	**Russian Federation**						
Commodity	**Softwood Logs**				1000 CUBIC METERS		
	2003 USDA Official [Old]	Revised Post Estimate [New]	2004 USDA Official [Old]	Estimate Post Estimate [New]	2005 USDA Official [Old]	Forecast Post Estimate [New]	UOM
Market Year Begin		01/2003		01/2004		01/2005	MM/YYYY
Production	68000	71100	0	72500	0	74000	1000 CUBIC METERS
Imports	0	0	0	0	0	0	1000 CUBIC METERS
TOTAL SUPPLY	68000	71100	0	72500	0	74000	1000 CUBIC METERS
Exports	22500	27500	0	28050	0	28600	1000 CUBIC METERS
Domestic Consumption	45500	43600	0	44450	0	45400	1000 CUBIC METERS
TOTAL DISTRIBUTION	68000	71100	0	72500	0	74000	1000 CUBIC METERS

Table 3. Production, Supply, and Distribution of Temperate Hardwood Logs

PSD Table							
Country	**Russian Federation**						
Commodity	**Temperate Hardwood Logs**				1000 CUBIC METERS		
	2003 USDA Official [Old]	Revised Post Estimate [New]	2004 USDA Official [Old]	Estimate Post Estimate [New]	2005 USDA Official [Old]	Forecast Post Estimate [New]	UOM
Market Year Begin		01/2003		01/2004		01/2005	MM/YYYY
Production	24000	23800	25500	25500	0	26800	1000 CUBIC METERS
Imports	0	0	0	0	0	0	1000 CUBIC METERS
TOTAL SUPPLY	24000	23800	25500	25500	0	26800	1000 CUBIC METERS
Exports	10000	8995	10000	9715	0	10300	1000 CUBIC METERS
Domestic Consumption	14000	14805	15500	15785	0	16500	1000 CUBIC METERS
TOTAL DISTRIBUTION	24000	23800	25500	25500	0	26800	1000 CUBIC METERS

Table 4. Production, Supply, and Distribution of Softwood Lumber

PSD Table

Country	**Russian Federation**						
Commodity	**Softwood Lumber**				1000 CUBIC METERS		
	2003 USDA Official [Old]	Revised Post Estimate [New]	2004 USDA Official [Old]	Estimate Post Estimate [New]	2005 USDA Official [Old]	Forecast Post Estimate [New]	UOM
Market Year Begin		01/2003		01/2004		01/2005	MM/YYYY
Production	14665	14665	15400	15400	0	16250	1000 CUBIC METERS
Imports	0	0	0	0	0	0	1000 CUBIC METERS
TOTAL SUPPLY	14665	14665	15400	15400	0	16250	1000 CUBIC METERS
Exports	4750	4750	5225	5225	0	5485	1000 CUBIC METERS
Domestic Consumption	9915	9915	10175	10175	0	10765	1000 CUBIC METERS
TOTAL DISTRIBUTION	14665	14665	15400	15400	0	16250	1000 CUBIC METERS

Table 5. Production, Supply, and Distribution of Temperate Hardwood Lumber

PSD Table

Country	**Russian Federation**						
Commodity	**Temperate Hardwood Lumber**				1000 CUBIC METERS		
	2003 USDA Official [Old]	Revised Post Estimate [New]	2004 USDA Official [Old]	Estimate Post Estimate [New]	2005 USDA Official [Old]	Forecast Post Estimate [New]	UOM
Market Year Begin		01/2003		01/2004		01/2005	MM/YYYY
Production	4795	4790	4890	4890	0	5040	1000 CUBIC METERS
Imports	0	0	0	0	0	0	1000 CUBIC METERS
TOTAL SUPPLY	4795	4790	4890	4890	0	5040	1000 CUBIC METERS
Exports	400	215	420	235	0	260	1000 CUBIC METERS
Domestic Consumption	4395	4575	4470	4655	0	4780	1000 CUBIC METERS
TOTAL DISTRIBUTION	4795	4790	4890	4890	0	5040	1000 CUBIC METERS

Table 6. Production, Supply, and Distribution of Softwood Plywood

PSD Table

Country	**Russian Federation**						
Commodity	**Softwood Plywood**				1000 CUBIC METERS		
	2003 USDA Official [Old]	Revised Post Estimate [New]	2004 USDA Official [Old]	Estimate Post Estimate [New]	2005 USDA Official [Old]	Forecast Post Estimate [New]	UOM
Market Year Begin		01/2003		01/2004		01/2005	MM/YYYY
Production	270	270	275	275	0	281	1000 CUBIC METERS
Imports	2	2	2	2	0	2	1000 CUBIC METERS
TOTAL SUPPLY	272	272	277	277	0	283	1000 CUBIC METERS
Exports	186	186	190	190	0	194	1000 CUBIC METERS
Domestic Consumption	86	86	87	87	0	89	1000 CUBIC METERS
TOTAL DISTRIBUTION	272	272	277	277	0	283	1000 CUBIC METERS

Table 7. Production, Supply, and Distribution of Hardwood Plywood

PSD Table

Country	**Russian Federation**						
Commodity	**Hardwood Plywood**				1000 CUBIC METERS		
	2003 USDA Official [Old]	Revised Post Estimate [New]	2004 USDA Official [Old]	Estimate Post Estimate [New]	2005 USDA Official [Old]	Forecast Post Estimate [New]	UOM
Market Year Begin		01/2003		01/2004		01/2005	MM/YYYY
Production	1450	1700	1500	1800	0	1900	1000 CUBIC METERS
Imports	0	0	0	0	0	0	1000 CUBIC METERS
TOTAL SUPPLY	1450	1700	1500	1800	0	1900	1000 CUBIC METERS
Exports	920	1250	950	1325	0	1400	1000 CUBIC METERS
Domestic Consumption	530	450	550	475	0	500	1000 CUBIC METERS
TOTAL DISTRIBUTION	1450	1700	1500	1800	0	1900	1000 CUBIC METERS